California Actuarial Advisory Panel
Defining the Range of Actuarial Model Policies and Best Practices for Public Retirement Plan Funding

Note: The "Best Practices" are meant to be illustrative and not necessarily the recommendations of the subcommittee.

Objectives: Define "Best Practice" Actuarial Funding Methods

- Actuarial methods allocate the total cost of the pension plan to appropriate periods
- Volatility should be minimized without compromising underlying cost
- Pay-related benefit costs should reflect anticipated pay at determination
- No gains or losses should occur if all assumptions are met
- Actuarial value of assets should reflect market value
- Gains or losses (changes in unfunded liability) should be amortized over a reasonable time period
- New liabilities should be amortized over a reasonable time period
- Each participant's benefit should be funded under a reasonable allocation method by projected termination date
- Current assets and future contributions should be sufficient to pay all benefits to current active, inactive and retired participants

Best Practices – Actuarial Funding Methods – the determination of how much of the total value of the members' future benefits should be contributed/allocated to each plan year

- Pay-related benefit plans
  - Entry age normal cost – spreads the cost more evenly across the years and typically is more stable
  - Projected unit credit
- Plans not pay related
  - Projected unit credit
  - Unit credit
- Individual account plans
  - Unit credit

Best Practices - Unfunded Actuarial Accrued Liability Amortization Policy – defines the method (length of time and structure) to pay off the unfunded actuarial accrued liability obligation over time

- Type
  - Level percent of pay or level dollar amount
- Period
  - Not greater than a 30-year fixed period
  - Gains/losses, plan changes, and method and assumption changes should be amortized over a new period not to exceed 30 years
  - Retroactive benefit increases should be amortized over a shorter period

   - Surpluses should be amortized in the same manner

Best Practices – Asset Valuation Methods - a method to minimize the impact of short-term, year-to-year investment performance fluctuations on contributions

- Actuarial value of assets must be market related
   - Actuarial value of assets must be between 80% and 120% of market value
   - The wider the corridor, the more stable the contribution
- Unrecognized investment gains/losses must be spread/recognized over a period not to exceed five years
- The expected rate of return should reflect the long-term expected return on the assets the plan will invest in

Practices Deemed to be Unreasonable

- Gains or losses generated if all assumptions are met
- Unfunded actuarial liability not expected to be reduced over time
- Contributions increase (as a percent of payroll or per participant) over time